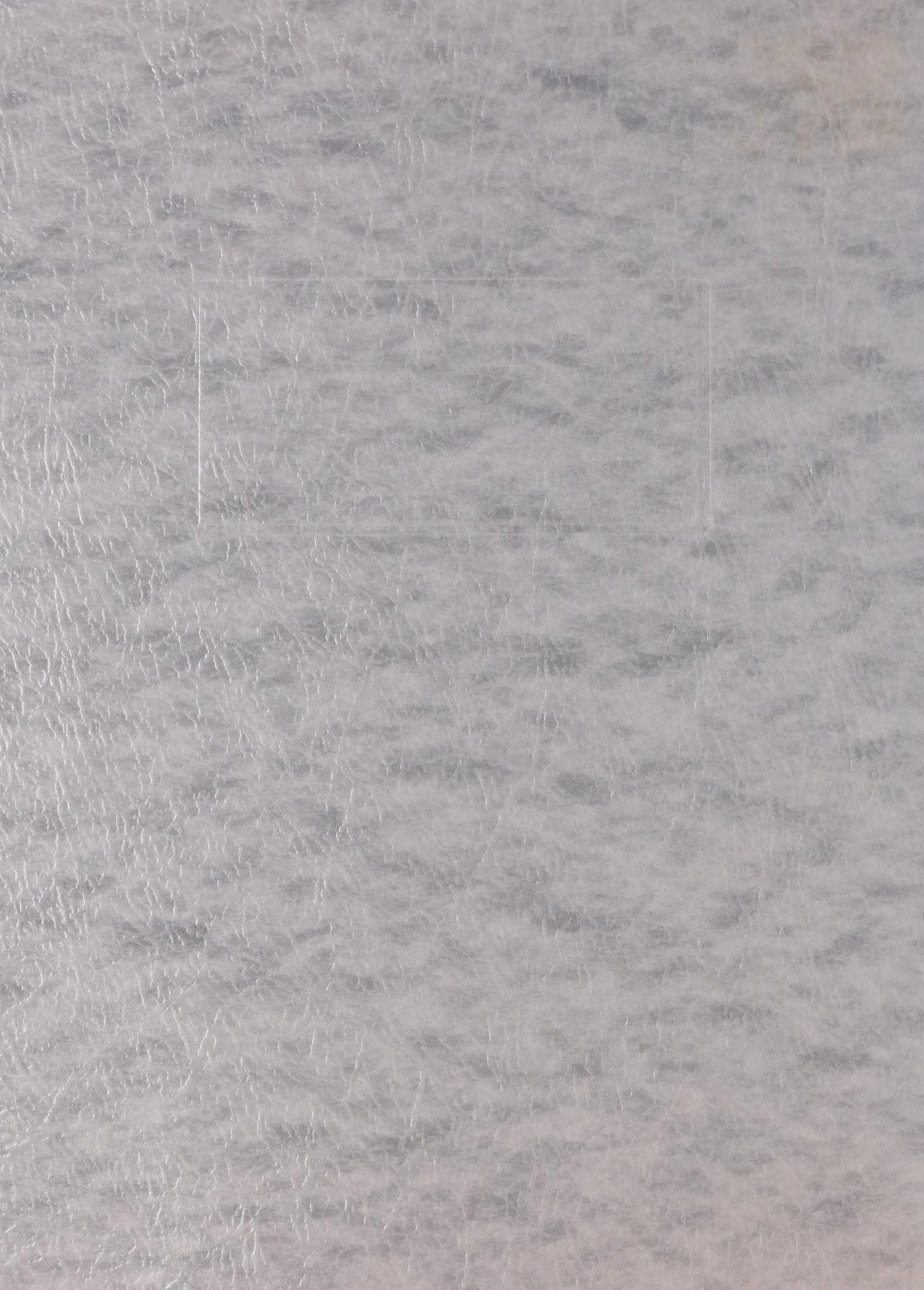


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### REDUCTION OF TARIFFS ON SUPPLY-MANAGED COMMODITIES UNDER THE GATT AND THE NAFTA



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## **REDUCTION OF TARIFFS ON SUPPLY MANAGED COMMODITIES UNDER THE GATT AND THE NAFTA**

### **INTRODUCTION**

Currently, Canada strictly limits the quantities of dairy products, poultry and eggs that can be imported. Without such import quotas, domestic supply management programs for these products would be ineffective in raising prices since imports would be drawn in to satisfy domestic demand.

Authorization for these quotas is provided under Article XI:2(c)(i) of the General Agreement on Tariffs and Trade ("GATT"), which permits import restrictions on agricultural and fisheries products "necessary to the enforcement of governmental measures which operate: (i) to restrict the quantities of the like domestic product" to be marketed or produced.

Under the terms of the GATT Uruguay Round agreement reached in December 1993, quotas on agricultural imports must be converted into their tariff equivalents by 1 July 1995 and reduced over a six-year period commencing in 1995 by a minimum rate of 15% per product. Overall, tariffs on agricultural goods, including tariff equivalents, must be decreased by 36% over the six years. To fulfil its obligations under the GATT agreement, the Canadian government is proposing to replace its system of import quotas for poultry, eggs and dairy products with tariffs.

Under the terms of the North American Free Trade Agreement ("NAFTA"), however, the Parties are required to eliminate duties on each other's goods. Canada-U.S. trade is governed by the tariff phase-out schedule of the Canada-United States Free Trade Agreement ("CUSTA"). Under the CUSTA, tariffs are to be eliminated according to three arrangements: a) immediately; b) over five years; or c) over ten years.

The conflict between the GATT tariff reduction provisions (15% per tariff item over six years - 36% overall) and the NAFTA/CUSTA requirement for the complete elimination of all Canada-U.S. tariffs by 1998 raises questions as to which agreement takes precedence.

The Canadian and U.S. governments have differing views on the matter. Canada takes the position that the GATT tariff reduction provisions prevail, while the U.S. contends that the tariffs imposed under the GATT will have to be reduced and eventually eliminated in accordance with the NAFTA. The following discussion reviews the relevant GATT and NAFTA articles and raises some of the possible arguments on both sides of the issue.

## TARIFFICATION UNDER THE URUGUAY ROUND

In the Agreement on Agriculture concluded in the Uruguay Round multilateral trade negotiations, Parties agreed among other things, to convert all non-tariff barriers to tariffs by 1 July 1995. Article 4(2) of this Agreement provides that:

Members shall not maintain, resort to, or revert to any measures of the kind which have been required to be converted into ordinary customs duties, except as otherwise provided for in Article 5 and Annex 5 hereof.<sup>(1)</sup>

A footnote accompanying Article 4 notes that measures that must be converted into customs duties include quantitative import restrictions. Other documentation flowing from the Uruguay Round clearly states that import quotas are to be transformed into tariff equivalents.<sup>(2)</sup>

The Canadian government proposes that the tariff equivalent of existing quotas should amount to 283.8% for milk, 351.4% for butter, 289% for cheddar cheese, 280.4% for chicken and 192.3% for eggs.

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(1) Agreement on Agriculture, MTN/FA II-A1A-3, Article 4.

(2) Modalities for the Establishment of Specific Binding Commitments under the Reform Programme, MTN.GNG/MA/W/24, Annex 3.

## PRECEDENCE OF THE NAFTA OR THE GATT WITH RESPECT TO THE GATT TARIFFICATION MEASURES

### A. Canada-U.S. Trade

Throughout the NAFTA, there are numerous references to the GATT. Article 103(2) of the NAFTA establishes the principle that the NAFTA takes precedence over the GATT and other agreements to which Canada, Mexico and the United States are signatories, except where the NAFTA provides otherwise. Thus, for the GATT tariffication requirement and consequent reduction schedule to prevail over the NAFTA tariff elimination provisions, the NAFTA must recognize the GATT requirements as an exception to the general NAFTA provisions.

As mentioned earlier, under the GATT, import tariffs are to replace non-tariff barriers on agricultural products, and all tariffs, including those imposed as a result of tariffication, are to be reduced over a period of six years from 1995 to 2001 by a minimum of 15% per product or 36% overall. The NAFTA, on the other hand, prohibits Canada and the United States from increasing any existing customs duty or adopting any new customs duty unless the Agreement otherwise provides and requires tariffs on agricultural products to be eliminated by 1 January 1998 (Articles 302(1) and (2)).

However, the scope and coverage of Article 302, indeed all of Chapter 3 of the NAFTA, is restricted explicitly by the Chapter's first provision, which allows for exceptions to the NAFTA's market access and tariff elimination provisions. Article 300 provides that:

This Chapter applies to trade in goods of a Party, including: ...  
(c) goods covered by another Chapter in this Part,  
except as provided in such ... Chapter.

The NAFTA chapter governing trade in agricultural goods is Chapter 7. At the outset, Article 701(2) establishes the primacy of the sections dealing with agriculture over other provisions of the NAFTA in the event of inconsistencies.

The specifics of agricultural trade between the Parties are set out in Annexes to the Chapter. Annex 702.1 incorporates into the NAFTA a series of CUSTA provisions dealing

with agricultural trade between Canada and the United States, including CUSTA Article 710. This article refers to Canada's rights and obligations under the GATT and states:

Unless otherwise specifically provided in this Chapter, the Parties retain their rights and obligations with respect to agricultural, food, beverage and certain related goods under the *General Agreement on Tariffs and Trade* (GATT) and agreements negotiated under the GATT,<sup>(3)</sup> including their rights and obligations under GATT Article XI.

Paragraph 4 of Annex 702.1 amplifies this provision by stating that Canada and the U.S. understand that CUSTA Article 710 incorporates their GATT rights and obligations with respect to agricultural trade. Thus, by incorporating CUSTA Article 710 into its provisions, the NAFTA makes Canada's obligations respecting agricultural trade under the GATT and agreements negotiated under the GATT a component of the NAFTA.

But what if these GATT obligations conflict with the market access and tariff elimination provisions of Chapter 3 of NAFTA? As previously noted, Article 300 of NAFTA permits Article 302 to be circumscribed by the provisions of other Chapters of the NAFTA and Article 701(2) makes Chapter 7 paramount where there is an inconsistency with other NAFTA provisions. Moreover, international treaty law provides that when one treaty, in this case the NAFTA, explicitly states that it is subject to the provisions another treaty, as the NAFTA does with the GATT, the other treaty prevails in the event of a conflict.<sup>(4)</sup> As a result, it would appear that the GATT rights and obligations maintained under CUSTA Article 710 could override both the NAFTA prohibition on the creation of new customs duties and its tariff elimination schedule.

While it can be argued that Canada's GATT rights and obligations are incorporated into the NAFTA and may prevail in the event of a conflict with the NAFTA, an important remaining question is what particular GATT rights and obligations are incorporated: are they those in existence before the NAFTA came into force or those that might arise after the

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(3) Emphasis added.

(4) Vienna Convention on the Law of Treaties Between States and International Organizations or Between International Organizations, Article 30(2).

NAFTA became operative? In other words, does the recent Uruguay Round Agreement on Agriculture, even though it comes into effect after NAFTA, qualify as an agreement negotiated under the GATT that would be incorporated into NAFTA by virtue of CUSTA Article 710? This involves a determination of whether the phrase "agreements negotiated under the GATT" referred to in CUSTA Article 710 covers prospective as well as existing GATT agreements.

In this regard, Article 103(1) of NAFTA is instructive. Under this Article, the Parties affirm their "existing" GATT rights and obligations, that is, their rights and obligations in effect on 1 January 1994.<sup>(5)</sup> However, neither CUSTA Article 710 nor Annex 702.1(4), which incorporate into the NAFTA the GATT rights and obligations of Canada and the United States, is qualified by the word "existing." Thus, it could be argued that the GATT rights and obligations incorporated into the NAFTA are prospective and therefore include those agreed to at the Uruguay Round.

Article 309(1) of NAFTA, which deals with quantitative restrictions on imports and exports, could also lend support for the argument that future GATT rights and obligations are incorporated into the NAFTA. It provides as follows:

Except as otherwise provided in this Agreement, no Party may adopt or maintain any prohibition or restriction on the importation of any good of another Party or on the exportation or sale for export of any good destined for the territory of another Party, except in accordance with Article XI of the GATT, including its interpretative notes, and to this end Article XI of the GATT and its interpretative notes, or any equivalent provision of a successor agreement to which all Parties are Party, are incorporated into and made part of this Agreement.

Since Article 309 provides for the incorporation into the NAFTA of successor agreements to GATT Article XI, it could be argued that the provisions of the Uruguay Round agreement on the tariffication of import quotas and the accompanying tariff reductions are equivalent provisions of a successor agreement to Article XI and are therefore incorporated into the NAFTA. More generally, it could be argued that because Article 309 and other NAFTA

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(5) According to Article 201(1) of the NAFTA, "existing" rights and obligations are those in effect when the NAFTA comes into force.

articles clearly contemplate future GATT agreements, it would not be logical for the NAFTA agriculture provisions to apply only to GATT obligations in force prior to 1 January 1994.

On the other hand, these same provisions might be used to support a position favouring the precedence of the NAFTA tariff reduction schedule. Contrary to the argument presented above, it could be asserted that Article 309 was intended to govern trade barriers of a quantitative nature rather than customs tariffs. Article 309 is similar in language to GATT Article XI, which is entitled "General Elimination of Quantitative Restrictions." Furthermore, Article 309 is found in the Chapter 3 of the NAFTA under, "Section C - Non-Tariff Measures." It is not clear from the text of the Article that the negotiators intended to sanction successor agreements to GATT Article XI other than those of a quantitative nature. Article 309 proscribes import and export restrictions unless they accord with Article XI of the GATT and it is "to this end"<sup>(6)</sup> that the NAFTA incorporates Article XI or any equivalent provision of a successor agreement. The "end" or purpose to which Article 309 refers is that of limiting the use of quantitative restrictions to the special cases provided for in GATT Article XI and successor agreements. As a result, it could be argued that Article 309 would not support the imposition and maintenance of customs duties under the Canadian tariffication proposal.

The fact that some provisions of the NAFTA, such as Article 309, specifically refer to future GATT agreements might be used to support arguments against the position that NAFTA incorporates the tariffication and tariff elimination provisions of the Uruguay Round. It might be contended that the absence of any specific reference to future or successor agreements in Annex 702.1, when such references are included in other NAFTA Articles, could be interpreted to mean that the NAFTA contemplates only current GATT obligations.

## B. Canada-Mexico Trade

The elimination of tariffs with Mexico is covered under Article 302 and Annex 302.2 of NAFTA, which provide for a maximum phase-out period of 15 years. In fact, all Canadian tariffs against Mexican goods will be eliminated by 1 January 2003. Duties on

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(6) Emphasis added.

poultry, egg and dairy products, however, are exempt from the general tariff elimination provisions (Article 703(2) and Annex 703.2).

Under Annex 703.2, Canada and Mexico have agreed to incorporate into NAFTA their rights and obligations with respect to agricultural goods under the GATT and agreements negotiated under the GATT, including their rights and obligations under GATT Article XI. The Annex also provides that either Canada or Mexico may adopt or maintain a prohibition or restriction or a customs duty on the importation of poultry, egg and dairy products originating from the other.

### **C. Dispute Settlement**

Unless Canada and the United States can agree to settle any disagreement over tariff reductions on supply managed goods, formal dispute settlement procedures are likely to be initiated. Chapter 20 of the NAFTA establishes a dispute settlement procedure in connection with disputes that may arise over the interpretation or application of the Agreement or when a Party considers a measure to be inconsistent with the obligations of the Agreement or to cause nullification or impairment (Article 2004).

A dispute over the introduction or reduction of tariffs on supply managed goods would likely fall under the Chapter 20 dispute settlement provisions, since it relates to the interpretation or application of the NAFTA. The U.S. might also claim that Canada's refusal to eliminate tariffs on these goods is inconsistent with the obligations of the NAFTA and thus causes nullification or impairment of the benefits the U.S. expected to receive under the Agreement.

The NAFTA, however, does not preclude dispute settlement under the GATT. Generally, disputes that may arise under both the NAFTA and the GATT may be settled in either forum at the discretion of the complaining Party, which, if it wishes to initiate a GATT dispute settlement proceeding, it must notify any third Party of its intention. Should the third Party wish to have recourse to the dispute settlement procedure regarding the matter, it and the complaining Party must decide on a single forum. If they are unable to agree, the dispute must normally be decided under the NAFTA (Article 2005(2)). Once dispute settlement procedures

have been initiated under the GATT or Chapter 20 of NAFTA, however, the forum cannot be changed.

## CONCLUSION

Unless the NAFTA provides otherwise, it takes precedence over the GATT. The NAFTA does not specifically provide Canada with the right to maintain or adopt customs duties on dairy, poultry and egg products imported from the U.S. Thus, to support its position on tariffication and the reduction of tariffs according to the GATT Uruguay Round Agreement, Canada must rely on certain provisions of the NAFTA (e.g., Article 309) and the CUSTA (e.g., Article 710) as well as general principles of international law.

A case can be made to support the view that Canada has the right to apply tariffs in accordance with the Uruguay Round Agreement on Agriculture. Nevertheless, the U.S. position that the NAFTA takes precedence over the GATT in the matter of tariff reductions cannot be discounted.







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